



Dave Yost • Auditor of State

MANAGEMENT LETTER

City of Macedonia
Summit County
9691 Valley View Road
Macedonia, Ohio 44056

To the Honorable Mayor and City Council:

We have audited the financial statements of City of Macedonia, Summit County, (the City) in accordance with *Government Auditing Standards*, as of and for the year ended December 31, 2011, and have issued our report thereon dated September 28, 2012.

Government Auditing Standards require us to report significant internal control deficiencies, fraud, and illegal acts (including noncompliance with laws and regulations), and also abuse and noncompliance with contracts and grant agreements that could directly and materially affect the determination of financial statement amounts. We have issued the required report dated September 28, 2012, for the year ended December 31, 2011.

We are also submitting the following comments for your consideration regarding the City's compliance with applicable laws, regulations, grant agreements, contract provisions, and internal control. These comments reflect matters that do not require inclusion in the report *Government Auditing Standards* require. Nevertheless, these comments represent matters for which we believe improvements in compliance or internal controls or operational efficiencies might be achieved. Due to the limited nature of our audit, we have not fully assessed the cost-benefit relationship of implementing these recommendations. However, these comments reflect our continuing desire to assist your City. If you have questions or concerns regarding these comments please contact your regional Auditor of State office.

Noncompliance Findings

- *1. **Ohio Rev. Code Section 5705.41(D)** requires that no subdivision or taxing unit shall make any contract or give any order involving the expenditure of money unless there is attached thereto a certificate of the fiscal officer of the subdivision that the amount required to meet the obligation has been lawfully appropriated for such purpose and is in the treasury or in the process of collection to the credit of an appropriate fund free from any previous encumbrances. This certificate need be signed only by the subdivision's Finance Director. Every contract made without such a certificate shall be void, and no warrant shall be issued in payment of any amount due thereon.

There are several exceptions to the standard requirement stated above that a Finance Director's certificate must be obtained prior to a subdivision or taxing authority entering into a contract or order involving the expenditure of money. The main exceptions are: "then and now" certificates, blanket certificates, and super blanket certificates, which are provided for in sections 5705.41(D)(1) and 5705.41(D)(3), respectively, of the Ohio Revised Code.

Noncompliance Findings (Continued)

- A. "Then and Now" Certificate – If the Finance Director can certify that both at the time that the contract or order was made ("then"), and at the time that the Finance Director is completing the certification ("now"), that sufficient funds were available or in the process of collection to the credit of a proper fund, properly appropriated and free from a previous encumbrance, the City can authorize the drawing of a warrant for the payment of the amount due. The City has thirty days from the receipt of the "Then and Now" certificate to approve payment by ordinance or resolution.

Amounts of less than \$3,000 may be paid by the Finance Director without a resolution or ordinance upon completion of the "Then and Now" certificate, provided that the expenditure is otherwise lawful. This does not eliminate any otherwise applicable requirement for approval of expenditures by the City.

- B. Blanket Certificate – Finance Directors may prepare "blanket" certificates for a certain sum of money not in excess of an amount established by resolution or ordinance adopted by a majority of the members of the legislative authority against any specific line item account over a period not running beyond the end of the current fiscal year. The blanket certificates may, but need not, be limited to a specific vendor. Only one blanket certificate may be outstanding at one particular time for any one particular line item appropriation.
- C. Super Blanket Certificate – The City may also make expenditures and contracts for any amount from a specific line item appropriation account in a specified fund upon certification of the Finance Director for most professional services, fuel, oil, food items, and any other specific recurring and reasonably predictable operating expense. This certification is not to extend beyond the current year. More than one super blanket certificate may be outstanding at a particular time for any line item appropriation.

Three out of twenty-three (13%) of the expenditures tested were not certified by the Finance Director prior to incurring the obligation. Additionally, it was also found that none of the exceptions noted above were utilized for the items found to be in noncompliance.

Unless the exceptions noted above are utilized, prior certification is not only required by statute but is a key control in the disbursement process to assure that purchase commitments receive prior approval. To improve controls over disbursements and to help reduce the possibility of the City's funds exceeding budgetary spending limitations, the Finance Director should certify the funds are, or will be available, prior to the obligation by the City. When prior certification is not possible, "Then and Now" certification should be used.

2. **Ohio Rev. Code Section 5705.36 (A)(1)** requires that on or about the first day of each fiscal year, the fiscal officer of each subdivision shall certify to the county auditor the total amount from all sources available for expenditures from each fund set up in the tax budget. The amount certified shall include any unencumbered balances that existed at the end of the preceding year, excluding any of the following:
- (a) Any reserve balance in an account established under section 5705.13 of the Revised Code for the purpose described in division (A)(1) of that section;
 - (b) The principal of a nonexpendable trust fund established under section 5705.131 of the Revised Code and any additions to principal arising from sources other than the reinvestment of investment earnings arising from that fund;

Noncompliance Findings (Continued)

2. Ohio Rev. Code Section 5705.36 (A)(1) (Continued)

(c) The balance in a reserve balance account established under section 5705.132 of the Revised Code.

The City prepared the Certificate of the Total Amount From All Sources Available for Expenditures and Balances in March 2011 but did not submit it to the County for certification. Additionally, the City has an Emergency Reserve Fund established under 5705.13 with an unencumbered balance of \$500,000 which was improperly included in the total amount available for expenditure.

To help maintain compliance with budgetary requirements the City should prepare the required Certificate of the Total Amount from All Sources Available for Expenditures and Balances on or about the first day of the year and submit it to the County Budget Commission for certification. Additionally, the Certificate should not include reserve balance accounts which are required to be excluded per the Ohio Revised Code.

3. **Ohio Rev. Code Section 5705.39** requires the total appropriations from each fund shall not exceed the total of the estimated revenue available for expenditure there from, as certified by the budget commission, or in case of appeal, by the board of tax appeals. No appropriation measure shall become effective until the county auditor files with the appropriating authority a certificate that the total appropriations from each fund, taken together with all other outstanding appropriations, do not exceed such official estimate or amended official estimate. When the appropriation does not exceed such official estimate, the county auditor shall give such certificate forthwith upon receiving from the appropriating authority a certified copy of the appropriation measure. Appropriations shall be made from each fund only for the purposes for which such fund is established.” Final General Fund appropriations exceeded estimated resources by \$406,873.

The Finance Director and Council should closely monitor appropriations and estimated resources to help ensure appropriations do not exceed estimated resources.

4. **Ohio Rev. Code Section 5705.36(A)(3)** requires upon a determination by the fiscal officer of a subdivision that the revenue to be collected by the subdivision will be greater than the amount included in an official certificate and the legislative authority intends to appropriate and expend the excess revenue, the fiscal officer shall certify the amount of the excess to the commission, and if the commission determines that the fiscal officer's certification is reasonable, the commission shall certify an amended official certificate reflecting the excess.

The City's expected revenues were higher than the amount included on the Certificate of Estimated Resources as certified by the County Budget Commission and the City's intention was to expend the additional revenue as evidenced by the fact that appropriations approved by Council exceeded budgeted revenue on the amended certificate of estimated resources. However, the Finance Director did not request an amended certificate of estimated resources certifying the excess.

To help ensure compliance with budgetary requirements, the City should request an amended certificate of estimated resources from the County Budget Commission when revenue is expected to exceed current estimates and the excess is intended to be appropriated and spent.

Recommendations

*1. Income Taxes Receivable

A portion of the City's Income Taxes Receivable was recorded net of the retainer (\$18,874) for January 2012 (received by the City in February 2012) as a result of the Generally Accepted Accounting Principles (GAAP) Conversion team utilizing net amounts for income tax revenue from the Regional Income Tax Agency (RITA). Additionally, December 2011 income tax collections for the Macedonia/Northfield Center Joint Economic Development District, \$18,617, (received in January 2012) were not included in the calculation of the Income Tax Receivable for the JEDD share nor did the City record an Intergovernmental Revenue and Undistributed Monies for their portion of the JEDD income tax. Lastly, December 2011 RITA City Monthly Distribution Report was not available, consequently, the GAAP Conversion team used the Detail Revenue Transaction Report provided to them by the Finance Director which reported \$428,891 total distribution as opposed to the December 2011 RITA City Monthly Distribution Report total distribution amount of \$489,077 of which \$419,237 (85.72%) should have been distributed to the General Fund and \$69,840 (14.28%) should have been distributed to the Family Recreation Center Fund. As result, Income Taxes Receivables were understated by \$51,591 within the General Fund and \$8,595 within the Family Recreation Center Fund.

The City should review the GAAP Conversion work papers to help ensure that Income Tax Receivable and Deferred Revenue amounts are properly stated and calculated using gross amounts and the calculation of the Income Tax Receivable includes all relevant amounts.

2. Northfield Center Distribution Agreement

The City has an agreement with Northfield Center Township (Township) regarding distribution of the income tax revenue for the Joint Economic Development Department (JEDD) that states income tax revenue for the JEDD remitted to the City and Township shall each equal 50% of the total net income tax generated. Said remittance shall be made to the Township quarterly for the prior three month period.

Distributions were made to the City and the Township in July of 2011 for the fourth quarter of 2010 as well as the first and second quarters of 2011. Another distribution was made in March of 2012 for the third and fourth quarter of 2011.

In order to uphold the agreement with the Township, the City should distribute the portion of the income tax revenue for the JEDD to the Township for the prior three month period every quarter.

3. Payments in Lieu of Taxes Receivables

During the generally accepted accounting principal (GAAP) conversion process, Payments in Lieu of Taxes Receivables (PILOT) receivable within the Tax Increment Financing Fund was calculated using an incorrect figure resulting in an understatement of PILOT receivable totaling \$285,510 and the related PILOT payable was not included at all, resulting in an understatement of PILOT payable (reported as Due to Other Governments on the financial statements) totaling \$307,530. The financial statements were adjusted to reflect this activity.

To help ensure accurate financial reporting the Finance Director should review all adjustments posted to the system, as well as receivable/payable calculations performed during the GAAP conversion process, for accuracy and proper recording.

Recommendations (Continued)

***4. Employee Manual**

City practice gives paid leave to its employees for birthdays, personal days, and comp time. However the City's employee manual contains no verbiage in regards to accrual and/or use of birthday and personal leave. Additionally, the manual is silent regarding if and how birthday, personal, and compensatory time leave balances should be paid out, as well as ambiguous as to proper calculation of sick leave payouts upon separation from service.

For ease of calculation and consistency of leave pay-outs, the City should update its employee manual to include verbiage relating to the accrual, use, and pay-out of birthday, personal, and compensatory time leave, as well as the pay-out of sick leave balances.

***5. Allocation of Income Tax Revenues**

The City's income tax ordinance identifies the allocation of net income tax proceeds by purpose; however, these purposes are not clearly defined in relation to the City's fund structure. As a result, determination of compliance with the ordinance is subject to interpretation and could be open to question.

The City should consider reviewing and revising the income tax ordinance to define the allocation percentages in terms which better correlate to the City's fund structure. This would assist in ensuring allocation of net income tax is performed in accordance with the City's intent.

6. Misposting and Misclassification of Revenues

The following receipts were improperly posted within the City accounting system and/or the financial statements by the Finance Director:

- Property Taxes were posted net of fees therefore understating Property Tax Revenue and related expenditures within the General Fund by \$83,980. Also, Property Taxes of \$133,338 were improperly classified as Intergovernmental Revenue instead of Property Tax Revenue within the General Fund.
- Property Taxes were posted net of fees therefore understating Property Tax Revenue and related expenditures within the Fire Protection Fund by \$8,327. Also, Property Taxes of \$22,460 were improperly classified as Intergovernmental Revenue instead of Property Tax Revenue within the Fire Protection Fund.
- Property Taxes were posted net of fees therefore understating Property Tax Revenue and related expenditures within the Police Pension Fund by \$3,010. Also, Property Taxes of \$15,093 were improperly classified as Intergovernmental Revenue instead of Property Tax Revenue within the Police Pension Fund.
- Special Assessments were posted net of fees therefore understating Special Assessment Revenue and related expenditures within the Special Assessment Bond Retirement Fund by \$4,297.
- The August 2011 Homestead and Rollback revenue was posted net of fees therefore understating Intergovernmental Revenue and related expenditures by \$767 within the General Fund, \$196 within the Fire Protection Fund, and \$61 within the Police Pension Fund.
- For the months of May through December, municipal income taxes were posted net of related fees resulting in understatements in the General Fund of both Municipal Income Tax Revenue and Income Tax Expenditures totaling \$149,303.

Recommendations (Continued)

6. Misposting and Misclassification of Revenues (Continued)

- For the months of May through December, municipal income taxes were posted net of related fees resulting in understatements in the JEDD Fund of both Municipal Income Tax Revenue and Income Tax Expenditures totaling \$4,780.
- The April 2011 income tax distribution was recorded twice resulting in the overstatement of Income Tax Revenue and related expenditures by \$23,630.
- JEDD Fund income tax refunds were improperly posted as revenue rather than reductions of revenue and offsetting amounts were recorded as expenditures resulting in overstatements of JEDD Fund income tax revenue and general government expenditures \$41,840.
- Although originally properly posted, when being brought into the new system, the January JEDD Fund income tax distribution was posted net of related fees and an offsetting amount was posted to reduce the properly recorded expenditures, resulting in understatements of JEDD Fund Income Tax revenue and General Government expenditures by \$430.
- Personal Property Reimbursements were improperly recorded as Real and Other Taxes, resulting in an understatement of Intergovernmental Revenue and overstatement of Real and other local tax revenue totaling \$165,647.

In order to help ensure accurate financial reporting, the City should post all receipts in the gross amount to the proper account.

7. Capital Assets

The following exceptions were identified during the testing of the City's fiscal year 2011 capital assets: (1) The City purchased 3 police cruisers during the year which were not included in the December 31, 2011 Capital Asset Summary, resulting in the understatement of capital assets by \$68,880. Additionally, the related depreciation expense for these assets was not included in the December 31, 2011 Depreciation Schedule, which understated depreciation expense by \$5,740; and (2) The City's Engineering Department identified \$17,380 of expenditures made during 2011 that should have been included in Construction In Progress as of December 31, 2011 but were not recorded.

In order to correct these deficiencies, the City should: (1) Ensure all qualifying assets are properly capitalized by including them in the Capital Asset Summary and are properly depreciated; and (2) Develop procedures to ensure all additions and deletions for CIP are recorded in the proper year.

***8. Disaster Recovery Plan**

In order to ensure minimal disruption to services, the City, including all outside collection points, should maintain a comprehensive disaster recovery plan that identifies procedures to perform which would permit the City to continue processing information in the event of a disaster. Data processing contingency plans identify arrangements for alternative data processing on compatible hardware and software. A proper plan removes as much time-consuming decision making as possible from the period immediately following the disaster.

Recommendations (Continued)

*8. Disaster Recovery Plan (Continued)

The City has not created a disaster recovery plan which documents the actions necessary to restore business operations in the event of a disaster which would temporarily or permanently disable the data processing capabilities of the City's financial related systems. Without a comprehensive disaster recovery plan there is a greater risk of loss of data, and an increased risk that computer operations important for the functioning of the City will not be restored in a timely, cost effective manner.

The City should develop a Disaster Recovery Plan. An elaborate plan is not necessary; however, an effective plan should be designed to ensure efficient recovery if a disaster occurs. We recommend, at a minimum, the following be completed:

1. Recovery Terms and Definitions
2. Technical (Hardware/Software) Recovery Procedures
3. End user Recovery Procedures
4. Readiness Plan
5. Emergency Contact List

Once completed, the contingency plan should be periodically reviewed and tested to ensure its continued applicability. This review should also ensure that personnel are sufficiently trained to carry out procedures necessary to restore functions critical to business operations. All individuals responsible for the disaster recovery plan tasks should retain a copy of the plan, and a copy of the plan should be kept off-site.

* We also reported these matters in our prior audit of the financial statements.

We intend this report for the information and use of the City Council, audit committee, and management.



Dave Yost
Auditor of State

September 28, 2012